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Bagley Corporation and Gerald H. Bagley v. Virginia Beach Federal Savings and Loan Association,Guaranty Northstate, Northstate Savings and Loan of Southern Pines, Atlantic Permanent Federal, Jefferson Savings and Loan, William T. Blair, Jr., William H. Bandy, Harry H. Knickerbocker, T. Linwood May, Nancy Bolten, John Livingstone, J. Rutherford, The Jeremy, Ltd., Jeremy Service Corporation, and Associated Title Company, Inc : Reply Brief

Utah Supreme Court

Original Brief Submitted to the Utah Supreme Court; digitized by the Howard W. Hunter Law Library, J. Reuben Clark Law School, Brigham Young University, Provo, Utah; machine-generated OCR, may contain errors.

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DOCKET NO. 88-0120-CA

IN THE SUPREME COURT OF THE STATE OF UTAH

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BAGLEY CORPORATION, a Utah corporation, and GERALD H. BAGLEY, an individual, individually and derivatively for and on behalf of THE JEREMY, LTD., a Utah limited partnership,	Supreme Court Appeal No. 860418
Plaintiffs/Appellants	Priority Classification 13b
vs.	
VIRGINIA BEACH FEDERAL SAVINGS AND LOAN ASSOCIATION, a foreign corporation, GUARANTY NORTHSTATE, fka NORTHSTATE SAVINGS AND LOAN OF SOUTHERN PINES, a foreign corporation, ATLANTIC PERMANENT FEDERAL, a foreign corporation, JEFFERSON SAVINGS & LOAN, a foreign corporation, WILLIAM T. BLAIR, JR., WILLIAM H. BANDY, HARRY H. KNICKERBOCKER, T. LINWOOD MAY, NANCY BOLTEN, JOHN LIVINGSTONE and J. RUTHERFORD, individuals, THE JEREMY LTD., a Utah limited partnership, JEREMY SERVICE CORPORATION, a Utah corporation, and ASSOCIATED TITLE COMPANY, INC., a Utah corporation,	District Court Civil No. 8725
Defendants/Respondents.	

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88-0120-CA

REPLY BRIEF OF APPELLANT

Appeal from an order dismissing plaintiff's derivative claims in the Third Judicial District, in and for Summit County, State of Utah, the Honorable Scott Daniels, District Court Judge, presiding.

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IN THE SUPREME COURT OF THE STATE OF UTAH

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BAGLEY CORPORATION, a Utah corporation, and GERALD H. BAGLEY, an individual, individually and derivatively for and on behalf of THE JEREMY, LTD., a Utah limited partnership, Plaintiffs/Appellants vs. VIRGINIA BEACH FEDERAL SAVINGS AND LOAN ASSOCIATION, a foreign corporation, GUARANTY NORTHSTATE, fka NORTHSTATE SAVINGS AND LOAN OF SOUTHERN PINES, a foreign corporation, ATLANTIC PERMANENT FEDERAL, a foreign corporation, JEFFERSON SAVINGS & LOAN, a foreign corporation, WILLIAM T. BLAIR, JR., WILLIAM H. BANDY, HARRY H. KNICKERBOCKER, T. LINWOOD MAY, NANCY BOLTEN, JOHN LIVINGSTONE and J. RUTHERFORD, individuals, THE JEREMY LTD., a Utah limited partnership, JEREMY SERVICE CORPORATION, a Utah corporation, and ASSOCIATED TITLE COMPANY, INC., a Utah corporation, Defendants/Respondents.	Supreme Court Appeal No. 860418 Priority Classification 13b District Court Civil No. 8725

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REPLY BRIEF OF APPELLANT

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ARGUMENT

1. The fact that limited partnerships are "creatures of statute" does not preclude this Court from recognizing the common law right of a limited partner to sue on behalf of the partnership.

Both the "Lenders" and Jeremy Service Corporation ("JSC") argue on appeal that because limited partnerships are "creature[s] of statute" that are granted express powers, "the courts cannot imply additional powers." See JSC's Brief, pp. 7-8; Lenders' Brief, pp. 6-7. That argument is not well taken. First, the argument is substantively incorrect -- the courts can imply, and, in fact have implied, powers of limited partnerships that are not expressly granted by statute. For example, this Court held that a limited partnership can sue in its own name. Wall Inv. Co. v. Garden Gate Distributing, 593 P.2d 542, 544 (Utah 1979). That power is not expressly provided in the Utah Limited Partnership Act, U.C.A. §48-2-1 et seq. (1953 as amended). Second, Hadlock v. Callister, 85 Utah 510, 39 P.2d 1082, 1085 (1935) cited by both defendants in support of the proposition that courts cannot imply powers not expressly granted to a limited partnership actually refutes that proposition. Hadlock does state that the grant of powers to corporations with respect to disposing of property "is limited by the express language of R.S. Utah 1933, 7-3-45 . . ." Id. However, Hadlock goes on to hold that a corporation also possesses "such implied powers as are necessary, usual or incidental to its business," so long as the implied powers are exercised in a proper manner.

Id. Finally, plaintiffs note that defendants' argument boils down to a contention that a technical rule should be blindly applied despite the private injustice and public injury that might result.

The fact that limited partnerships are "creatures of statute" does not preclude this Court from recognizing the limited partner's common law derivative right.

2. Neither the revisions to the Uniform Limited Partnership Act nor the Utah Legislature's failure to adopt those revisions prohibit the recognition of a limited partner's common law derivative right.

The Lenders and JSC both note that the 1976 revisions to the Uniform Limited Partnership Act expressly recognize the right of a limited partner to sue derivatively. See Lenders' Brief, p. 6, n. 1; JSC's Brief, p. 10; Uniform Limited Partnership Act (rev.) §§1001-1004. From this defendants argue that (1) it is therefore clear that the ULPA does not authorize derivative actions; and (2) some significance should be given to the fact that the Utah Legislature has not adopted the Revised Act. These arguments do not preclude the recognition of the common law derivative right of a limited partner.

Plaintiffs do not contend that the ULPA specifically authorizes derivative suits by limited partners. The relevant point is that the ULPA does not abolish a limited partner's common law derivative right. Thus, as explained in appellant's previous brief, the analysis shifts to a determination of whether the right of a limited partner to sue derivatively should be

recognized in accordance with public policy and the rules of statutory construction. Appellants respectfully submit that this question should be answered in the affirmative.

The inference defendants draw from the nonadoption of the RULPA is similarly flawed. The fact that the Utah Legislature has not adopted an express recognition of a limited partner's common law right does not mean that it has rejected it. The Legislature has only amended one section of the Utah Limited Partnership Act in the sixty-five years since its enactment. That amendment took place before the Uniform Act was revised. See Utah Code Ann. §48-2-13 (1953 as amended by L. 1975, ch. 139, §1). Legislative inaction is a weak reed on which to lean in determining legislative intent. Quinn v. State, 124 Cal.Rptr. 1, 539 P.2d 761 (1976); Barry v. Branner, 245 Or. 307, 421 P.2d 996 (1966).

Finally, insofar as the revisions to the Uniform Act are relevant to the issue of whether a limited partner can sue derivatively in Utah, those revisions indicate that such a right should be recognized by this Court. The fact that the RULPA expressly recognizes the common law derivative right provides testimony to the importance of the right. That fact also impugns the force of an argument that the right will conflict with the overall statutory scheme.

3. The common law derivative right does not conflict with the Utah Limited Partnership Act.

Lenders assert that the recognition of a limited partner's right to sue derivatively will provoke interference with the

management of limited partnerships. That argument ignores the inherent limitations on the right. Permitting limited partners to sue derivatively does not allow them to indiscriminately interfere in management because the right cannot be invoked until the limited partner has requested that the general partner take appropriate action and the general partner has then wrongfully refused to act on behalf of the partnership.

Lenders rely on Empire Investment Corp. & Associates v. Nielson Construction Co., 508 P.2d 804 (Utah, 1973) to support their argument that a limited partner should not have a derivative right. Defendants' reliance on Empire is misplaced. First, as defendants note, any statement in Empire concerning the rights of limited partners to sue on behalf of the limited partnership is purely dicta. The basis of the decision in Empire is that the issues in the case had been previously litigated and then settled. Second, even the dicta in Empire is not on point with respect to the issues involved in the instant case. The general partner in Empire had taken action on behalf of the partnership. In this case, the general partner refuses to do so. Finally, as this Court noted, the rights the limited partners may have had in Empire were purely personal rights and were solely against the general partner. Thus, Empire provides no authority for defendants' statement that §48-2-26 bars an action by limited partners on behalf of the partnership against third parties.

Defendants also point to 60 Am. Jur. 2d, "Partnership" §380, p.262, in support of their position. Lenders' Brief, page 9.

That section states that "the rights of a limited partner are generally confined to the rights to have full information" etc. Id. (emphasis supplied). The major fault in the defendants' reliance on that annotation is that they selectively read the provisions of Am. Jur. to make their point. Am. Jur. 2d also recognizes that there is an exception to the general rule: "a limited partner can bring an action on behalf of the partnership when the general partners have disabled themselves or wrongfully refuse to bring the action." 60 Am. Jur. 2d "Partnership" §390, pp. 270-271.

4. The common law derivative right of a limited partner is properly analogized to the derivative right of a corporate shareholder under the facts of the instant case.

Lenders' argument that "there are material differences between corporate shareholders and limited partners," is primarily based upon the fact that limited partners have a direct right against the general partner, while corporate shareholders have only a derivative right to protect themselves. See Lender's Brief p. 19. That argument fails under the facts alleged in plaintiffs' Amended Complaint. The Amended Complaint alleges that JSC, the general partner, is a "shell" corporation, which is grossly undercapitalized. Thus, plaintiffs' right to bring a direct action against JSC for JSC's breach of fiduciary duties is meaningless.

The Lenders also attack plaintiffs' analogy of the limited partner's common law derivative right to the derivative right of

corporate shareholders, stating that "[c]orporate shareholders have a statutory right to bring derivative claims. URCP 23.1." Lenders' Brief at p. 7, n. 2. Plaintiffs respond that, first, Rule 23.1 was adopted by the Supreme Court, not the Legislature, and, further, as discussed in detail in subpart 2, supra, the fact that there is no express statutory authorization for a limited partner to bring a derivative action does not preclude them from doing so.

5. Defendants Lenders' argument that Utah law does not permit joinder of direct and derivative claims in the same action is not properly before this court.

Lenders' Brief states that "[b]ecause no single reason was given for the trial court's ruling, respondents presume that the lower court considered and relied upon each of the grounds asserted in support of the Motion, and address those grounds separately herein." Lenders' Brief, p. 1. A review of the transcript of the hearing on the Motion to Dismiss reveals the inaccuracy of defendants' assertion.

At the close of plaintiffs' counsel's argument, the Court states: "assuming all that's true . . . still, I -- how do you get around the statute that says unless you are a general partner you're not a proper party from proceeding against the buyer [to a proceeding by or against the] of the partnership? I don't see how you read it any other way." Transcript at page 20. Similarly, the trial court stated: "I don't think it's really a question of rationale. I agree maybe there ought to be a limited partnership derivative suit, but I can't read this language any

other way. . . . I can't read this language saying anything else other than a limited partner can't be a -- bring against a partnership." Transcript at page 30. Though the transcript is garbled, the fact that the argument presented by plaintiffs' counsel centered solely on the existence of a derivative suit, coupled with the fact that the Court's Order dismissed only plaintiffs' derivative claims, rather than bifurcating plaintiffs' derivative and direct claims as would have been appropriate had the Court accepted defendants' joinder argument, make it clear that the sole basis for the lower court's decision was that Judge Daniels believed that U.C.A. §48-2-26 precluded derivative suits by limited partners. As the lower court did not rule on defendants' joinder argument, the determination of the issue is not before this Court. Plaintiffs respectfully submit that this issue should be properly determined by the lower court on remand, once the limited partners' derivative rights are recognized.

Even if defendants' joinder argument were properly before this court, the defendants' argument is not well taken. Defendants cite Goodliffe v. Colonial Corp., 155 P.2d 177, 182 (Utah 1945) as supporting the proposition that "it has long been the law in Utah that direct and derivative claims may not be joined in the same action." Lenders' Brief, at 16-17. In truth, Goodliffe holds that insofar "as direct relief to individual plaintiffs sought by them in a derivative suit is merely incidental to the restitution of property to the corporation, such individual relief may be granted in the same proceeding."

Id. (emphasis supplied). Goodliffe does note that in a derivative suit "those who champion the cause of action owned by the corporation cannot be permitted to assert in such a suit, claims hostile to the corporation and which are for their own exclusive benefit." Id. However, that does not preclude plaintiffs from bringing their direct and derivative claims together in this action. None of plaintiffs' direct claims in this action are adverse to the partnership's interests. The two claims that are purely personal to Gerald Bagley and Bagley Corporation, for defamation and conversion, are asserted solely against the Lenders and their alter ego, JSC. These claims are not adverse to, and will not affect, the partnership. However, because these claims arise out of the same conduct of the Lenders and JSC as the derivative claims, they are incidental to the derivative action and therefore are properly brought in the same action as the derivative suit under the Goodliffe "incidental" test. Defendants also cite Fanchon & Marco, Inc. v. Paramount Pictures, 107 F.Supp. 532, 540 (S.D.N.Y. 1952) to support their joinder argument. Plaintiffs note that the District Court's opinion in Fanchon & Marco was reversed by the Second Circuit Court of Appeals, 202 F.2d 731 (2nd Cir. 1953).

6. Defendant JSC's argument that plaintiffs lack standing to bring this action is not properly before this Court.

JSC's argument that plaintiffs lack standing to bring this action is not properly before this court. This argument was not before the lower court on the prior Motion to Dismiss. It is axiomatic that matters not presented to the trial court may not

be raised for the first time on appeal. Franklin Financial v. New Empire Dev. Co., 659 P.2d 1040, 1044 (Utah 1983).

CONCLUSION

Limited partners have a common law equitable right to sue on behalf of the partnership if the general partner wrongfully refuses or is unable to do so. The Utah Limited Partnership Act does not abolish that right. Therefore, the lower court's Order dismissing plaintiff's derivative claims on the basis that U.C.A. §48-2-26 prohibits such claims was error. Plaintiffs respectfully request that the Order of Dismissal be reversed and this case be remanded for further proceedings in the District Court.

DATED this 27th day of April, 1987.

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MAILING CERTIFICATE

The undersigned hereby certifies that four true and correct copies of the foregoing REPLY BRIEF OF APPELLANT were mailed, postage fully prepaid, on the 27th day of April, 1987 to each of the following:

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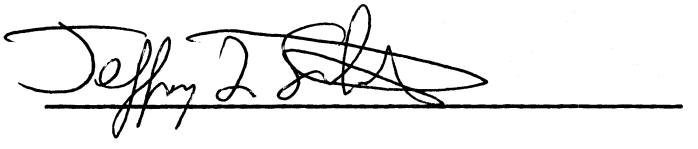

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